Hart Schaffner & Marx Annual Report -- 1976
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pg. 0_1

Hart Schaffner & Marx

Manufacturing and Retailing Quality Apparel

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	Clay E. Steele	*Retired (formerly Senior Vice President, Hart Schaffner & Marx)*

Corporate Staff	John R. Meinert	*Executive Vice President*
	Charles L. Stewart	*Vice President, Secretary and General Counsel*
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	Edward R. Weed	*Vice President*
	Mark J. Lies	*Treasurer*
	Jerome Dorf	*Controller*
	Roger H. Clausen	*Assistant Controller*
	Andrew A. Zahr	*Assistant Controller*
	Kay C. Nalbach	*Assistant Secretary*
	Harrison Hanson	*Director of Computer Systems*
	Ralph Kaufmann	*Director of International Licensing*
	William J. McNally, Jr.	*Director of Corporate Planning*

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Highlights

	Years ended November 30 1976	1975	Change
Net sales	**$534,609,000**	$486,833,000	+10%
Net earnings	**13,850,000**	8,310,000	+67%
Average number of common shares and common share equivalents	**8,588,000**	8,558,000	
Earnings per share	**1.61**	.97	+66%
Cash dividends per common share	**.63**	.60	+ 5%
Shareholders' equity	**179,473,000**	171,062,000	+ 5%
Equity per share	**20.97**	20.00	+ 5%

Employees	**20,500**	19,500	+ 5%
Shareholders	**8,900**	8,700	+ 2%
Retail stores in the U.S.	**261**	249	+ 5%

Quarterly Financial and Common Share Information

	Net Sales (000's Omitted)		*Net Earnings* (000's Omitted)		Per Share		*Cash Dividends* Per Share	
	1976	1975	**1976**	1975	**1976**	1975	**1976**	1975
First	**$136,836**	$128,039	**$4,050**	$2,580	**$.47**	$ 30	**$.15**	$.15
Second	**121,234**	115,604	**2,840**	1,707	**.33**	.20	**.15**	.15
Third	**127,628**	112,161	**2,580**	1,368	**.30**	.16	**.15**	.15
Fourth	**148,911**	131,029	**4,380**	2,655	**.51**	.31	**.18**	.15
Total	**$534,609**	$486,833	**$13,850**	$8,310	**$1.61**	$.97	**$.63**	$.60

Hart Schaffner & Marx common shares are traded under the symbol HSM on the New York and Midwest Stock Exchanges. The closing price on February 11, 1977 per common share was $14⅜ and the quarterly price range for the past two years was:

	Fiscal 1976				Fiscal 1975			
	Fourth	**Third**	**Second**	**First**	Fourth	Third	Second	First
High	**$13**	**$13**	**$14½**	**$12⅝**	$9¼	$10⅛	$9¼	$7
Low	**10¾**	**10**	**10¼**	**8**	8	8⅛	6⅞	4⅞

Series A cumulative preferred shares, on which quarterly $.50 cash dividends were paid in 1976 and 1975, while not separately traded, are each convertible into 1.8 common shares.

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Chicago, Illinois 60670

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New York City sales offices
1290 Avenue of the Americas,
New York, N.Y. 10019

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Hart Schaffner & Marx, with over 20,000 employees in 261 stores and 28 plants in the U.S., manufactures and retails quality apparel.

John D Gray Jerome S Gore

To Our Shareholders: Hart Schaffner & Marx, founded as a partnership in 1887 with a men's clothing store in Chicago, celebrates its ninetieth anniversary in 1977. Your Company has shown substantial growth through the years, and its prospects are excellent. We look forward to record sales and higher earnings to mark this anniversary year.

Consolidated sales reached a record high of $534,609,000 in the fiscal year ended November 30, 1976, an increase of 9.8 percent over the previous year's $486,833,000. Earnings increased 66.7 percent to $13,850,000 or $1.61 per share in 1976, from $8,310,000 or 97 cents per share in 1975, which was a depressed year for the Company and the apparel industry.

In view of the Company's improved earnings and bright prospects, your directors raised the quarterly dividend paid in November 1976, by 20 percent from 15 cents to 18 cents per share. The quarterly dividend of 18 cents per share paid in February 1977 marks our 38th consecutive year of dividends.

Retail Stores Division sales increased almost 9 percent to a record high of $337 million in the year ended November 30, 1976. Retail sales in December 1976 and January 1977, the first two months of our new fiscal year, increased 7 percent over last year's record sales. This increase, on top of a 10 percent sales increase for the same two months a year ago, was achieved despite the severe weather conditions. We expect retail sales to continue strong in 1977 because of the high level of personal income and improved consumer confidence.

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Sales of the manufacturing divisions also set a record in 1976. Total volume increased 13 percent to over $250 million, of which over $50 million was shipped to our own stores and is, therefore, excluded from consolidated sales. Sales to independent accounts also increased 13 percent to approximately $200 million, with increases in each of the six divisions. Orders for apparel marketed by the manufacturing divisions for spring 1977 are up approximately 10 percent and retailers are ordering early for fall 1977. Retailers' inventories are well in line and they are placing fall orders with confidence, strengthened by the excellent demand for our merchandise. We expect a successful fall season for our manufacturing divisions.

The fashion trend in men's apparel is toward classic elegance. There is a strong desire to be better dressed and this favors tailored clothing, which is our specialty. The renewed interest in suits, sport coats and slacks is especially pronounced in higher quality goods, which is the market served by our manufacturing and retail divisions. Most in demand is a suit with a vest, and the Hart Schaffner & Marx Clothes, Hickey-Freeman, M. Wile and Johnny Carson Apparel divisions are taking full advantage of this opportunity for increased volume. Jaymar-Ruby, the largest manufacturer of men's high-quality tailored slacks, has tripled its sales since it was acquired 10 years ago. It continues to expand in the sportswear market. Gleneagles manufactures quality rainwear and outerwear. This division had a sales increase in 1976, but experienced substantial markdowns, resulting primarily from leisure suits. Our Blue Jeans subsidiary enjoyed greatly improved sales in 1976.

The Retail Stores Division and the manufacturing divisions both contributed substantially to the higher consolidated earnings. Gross margins improved in both manufacturing and retailing. Expenses were carefully controlled and, as a result, both divisions had lower operating expense ratios to sales.

Interest expense decreased to $4,275,000 in 1976 compared to $6,614,000 in 1975. This $2,339,000 reduction, after taxes, improved earnings by 13 cents per share.

Return on investment improved to 8 percent in 1976. The retail and manufacturing divisions both improved but we are not satisfied with this rate of return. The Company has established aggressive long-term goals for further improvements in sales, earnings and return on investment. Objectives include developing our human resources to their full potential, creating marketing strategies to take full advantage of opportunities, and achieving a higher return on investment through a combination of better earnings and faster turnover of inventory.

Inventories are higher than a year ago because of higher sales and production levels. The ratio of inventories to sales in our retail stores is lower than it has been in many years. The increase in inventories is primarily in manufacturing because of increased orders; however, inventories are still below two years ago. It is necessary to plan further ahead for the purchase and receipt of piece goods to assure timely deliveries of our products to the retail trade.

Your Company is in excellent financial condition. Current assets are more than three times current liabilities. In anticipation of future growth, the Company entered into a 15-year, $25 million loan agreement with several insurance companies, to borrow $17 million in October 1976 and $8 million in May 1977. The long-term bank credit agreement was terminated in December 1976 when all remaining indebtedness to banks was paid. Shareholders' equity has increased to $20.97 per share or $179.5 million, which is more than three times long-term debt. With its financial capability, Hart Schaffner & Marx is in a position to take full advantage of its opportunities for further expansion, or for diversification, in both manufacturing and retailing.

The Company invested $9.3 million in fixed assets in 1976. Approximately $5 million was used to open 17 stores and for other improvements to retail locations. The Company now operates 261 stores and plans to open 12 to 14 more in 1977. Twenty-four stores, including four opened in 1976, are women's apparel stores. Women's wear volume now exceeds $85 million annually, and the Company is interested in enlarging this part of its business through internal growth and possible acquisitions. The manufacturing divisions accounted for approximately $4 million of fixed asset

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additions in 1976. The principal expenditure expanded the Jaymar-Ruby headquarters building in Michigan City, Indiana to add warehousing space and a cutting room with a new computerized grading and marking system.

The Company's international licensing program has proved to be very effective and we intend to expand in this important area. Licensing income continues to rise dramatically with the number of agreements and the licensees' sales. The Company provides apparel manufacturing and marketing know-how, along with the licensing of its brand names, to apparel manufacturers in Japan, Canada and several other countries. An extensive program with Marubeni Corporation, a major trading company, has met with enthusiastic acceptance in Japan, in the marketing of the Graham & Gunn, Ltd., Sterling & Hunt, Society Brand, Ltd., and Jaymar-Ruby brands. The Company also represents Jack Nicklaus and Johnny Carson in international licensing of men's apparel. Asahi Chemical Industry Co., Ltd. is the major licensee for Jack Nicklaus in Japan. The Johnny Carson name for clothing and furnishings and the Hickey-Freeman brand have been licensed in other countries. The strength of the Company's brand names and its expertise in apparel manufacturing and marketing will facilitate obtaining and developing qualified licensees in additional countries.

The Company owns a 4% interest in Austin Reed Group Ltd., which operates 66 stores in the United Kingdom and in Europe. As its licensee, the Hart Schaffner & Marx Clothes division produces and markets British-designed fashions in the United States under the name of Austin Reed of Regent Street.

In Mexico, the Company owns a majority interest in Robert's, which is included in the consolidated statements. This leading manufacturer-retailer of men's quality clothing operates 14 stores, of which the majority are in Mexico City. Robert's continues to grow in sales and earnings. However, a devaluation of the Mexican peso affected 1976 earnings for the Company by about 6 cents per share and, as a result, Robert's contributed 4 cents less per share than in the previous year.

Our present corporate and divisional organization was established almost 10 years ago as the best structure for managing and expanding our decentralized manufacturing, retailing and foreign operations. Merchandising direction and coordination between manufacturing and retailing result from frequent meetings and successful interaction among our divisional executives. They also meet quarterly with corporate officers to plan company policies and operations. A corporate system of financial, planning and budgetary controls establishes the framework within which each division has operating authority along with the responsibility for results. The corporate staff provides proficient services and company-wide direction in legal matters, leases, licensing, advertising and promotion, marketing research, insurance, taxation, computer systems and personnel practices. In addition, the Company's internal controls and procedures are strengthened by its experienced staff of internal auditors.

Our present organizational structure takes maximum advantage of the experience and abilities of our corporate and divisional executives and furthers the development of future management. During the past year, a substantial number of executives were promoted from within the organization and its divisions. Other experienced executives joined the company in responsible positions including Harry P. Guinther, executive vice president of the Retail Stores Division, Raymond L. Valentine, Jr., corporate vice president of operations and Ralph Kaufmann, director of international licensing.

James S. Bingay, a director of our Company since January 1974, died on July 30, 1976. Mr. Bingay, who was president and chief executive officer of The Mutual Life Insurance Company of New York, served on our board with distinction. We are saddened by his death and the valuable counsel of this warm friend will be greatly missed.

Our employees, our most important asset, make it possible for the Company to produce and market the finest quality apparel and to offer the best service to our customers. Our officers and directors join us in expressing our sincere appreciation to the dedicated people whose efforts achieve these results.

Very truly yours,

John D. Gray

John D. Gray
Chairman

Jerome S Gore

Jerome S. Gore
President and
Chief Executive Officer

February 11, 1977

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Our preferred brand names are featured in the marketing of a broad range of quality apparel.

Manufacturing

Hart Schaffner & Marx Clothes, our largest manufacturing division, produces Hart Schaffner & Marx, the best-known name in men's clothing, Jack Nicklaus sportswear, and other high quality clothing under the brand names of Society Brand, Ltd., Austin Reed of Regent Street, Graham & Gunn, Ltd. and Sterling & Hunt. The renowned Christian Dior collection is also tailored by Hart Schaffner & Marx. For spring 1977, Christian Dior Sport, a new line of semi-constructed, more casual clothing was introduced, styled and priced for the younger man. An enlarged line of Christian Dior Sport is being offered for the fall 1977 season. Society Brand, Ltd. offers unusual style and quality features and is sold by a select group of retailers.

Austin Reed of Regent Street specializes in British designed clothing which has broad appeal at prices below the Hart Schaffner & Marx range.

During 1976, the career apparel division, Fashionaire, was awarded substantial men's and women's uniform contracts from many companies, including United Airlines and McDonald's.

Hickey-Freeman is the largest U.S. manufacturer of superb quality men's tailored clothing. It competes in quality with the best custom tailoring in the world. Hickey-Freeman and Walter-Morton clothing is sold in the finest specialty and department stores in the country.

M. Wile is one of our most dynamic and fastest growing divisions. It produces Johnny Carson Apparel and the Rue Royale Collection by Nino Cerruti, which are unusually good fashion values at medium price levels. For fall 1977, the London International line with fine fabrics is being introduced for the young men's market. In addition, M. Wile produces private label clothing.

Jaymar-Ruby continues its rapid growth with Jaymar and famous Sansabelt branded slacks and has developed an outstanding line of sport suits, sport coats and coordinated sportswear. Beginning with fall 1977, it will also market a collection of slacks and coordinated sportswear designed by Nino Cerruti.

Blue Jeans Corporation features girls' and women's jeans and sportswear under store labels. Blue Jeans has developed a highly specialized styling approach and its Hallsboro and Corn Cobbers lines are enjoying great success.

The Gleneagles/Great Western division specializes in all-weather coats and casual outerwear. In addition to the famous Gleneagles raincoats, this division markets Johnny Carson, Christian Dior and Nino Cerruti raincoats and a broad line of Jack Nicklaus golf and boating jackets.

Thousands of the finest retail stores throughout the nation sell quality apparel with our famous brand names.

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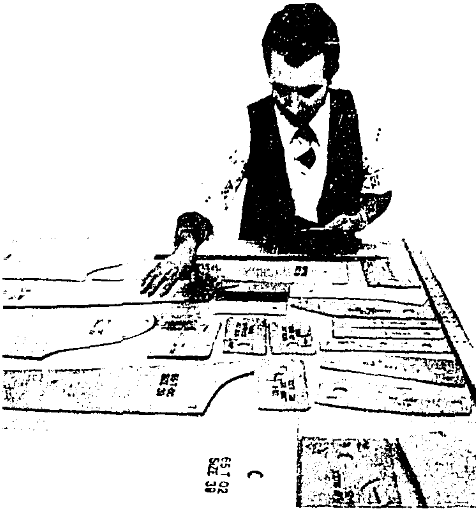
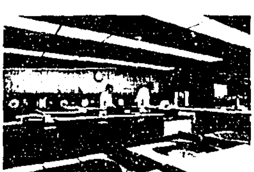
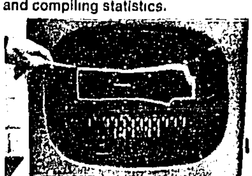
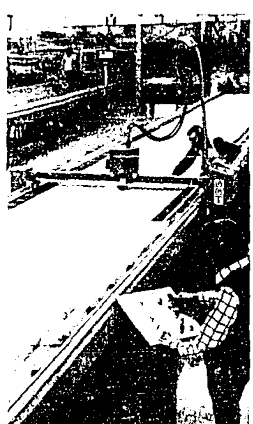


The designer creates the original garment pattern Master patterns, "graded" into a range of sizes, are made from this and then technology takes over. A master pattern, placed on a frosted glass table illuminated from below, is reproduced on photosensitive paper with an adhesive back This photo replica is then affixed to the surface layer of the "stack" of fabric, ready for cutting of the particular model and size directly through the paper

The space-age computer grading and marking system, similar to the system operating at our M Wile subsidiary in Buffalo, is introduced at the Jaymar-Ruby plant The system "grades" the designer's pattern in the range of sizes specified and makes paper patterns ready for cutting Or, it can make a tape which is fed into a digitized cutting machine to cut a "stack" of fabrics without the use of a pattern The manufacturing divisions also use computers for accounts receivable, woolen control, production scheduling and compiling statistics.







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Numerous pressings during the tailoring process augment stitching in shaping the component parts of a garment—canvas, lining, outer fabric—and molding them to the lines of the designer's original model.

Tailoring is the art of fashioning flat pieces of fabric into apparel that will fit the complex contours of the human body. Much of this shaping can be done by machines guided by skilled hands. In higher quality tailored garments, however, some details are "sculptured" entirely by hand, the "felling" (joining) of sleeve to armhole, or collar to shoulder, for examples. This is the province of gifted needleworkers, some of whom are second and third generation employees.

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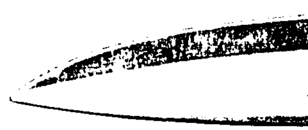
Our tailored garments are an expression of quality. Quality control begins with scrutiny of every inch of fabric and proceeds through every step of construction. Each individual operation must satisfy the critical eye of a control examiner. Only after passing its final inspection can completed garments be labeled with one of our brand names.

Patterned fabrics such as stripes and plaids require unusual finesse in cutting When the fabrics are spread on the cutting table in layers, the woven pattern in each layer must be precisely aligned with those above and below. The paper photo pattern is skillfully positioned on top so that the stripe or plaid will match and appear unbroken when joined at the seams or pockets of the completed garment



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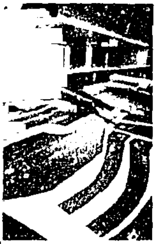
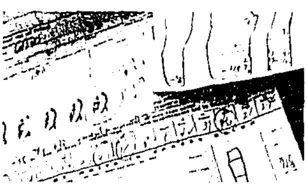






Discriminating men seeking individuality, and hard-to-fit customers are served by Custom Service departments. Measurements are taken by dealers' tailors, recorded on charts and forwarded. A master cutter analyzes the charts, alters the pattern as necessary and the individual garment is cut by hand. Upon completion, it is delivered to the dealer for minor fitting adjustments.

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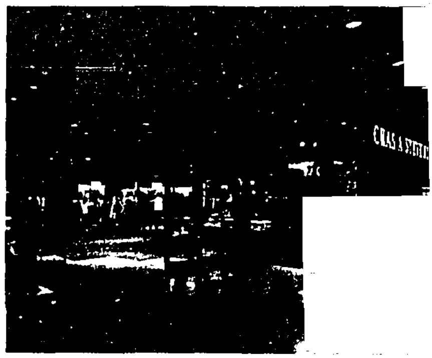
Chas. A. Stevens is the outstanding women's specialty store in the Chicago area. Shown here are new stores opened in 1976 in Water Tower Place on Michigan Avenue, and suburban Northbrook Court.



Millions of fashion-aware customers are served in our outstanding group of specialty stores.

Retail Stores

Your Company owns and operates 261 stores in 65 U.S. metropolitan areas and has a majority interest in Robert's with 14 stores in Mexico. Sales increased almost 9 percent to a record $337 million for 1976 compared to $310 million for the previous year. A further increase is expected for 1977.

The store names and locations are shown on pages 22 and 23 with the names of their top executives and the Retail Stores Division staff. Each retail subsidiary is an individual profit center operating under its own name, and its local management is guided by overall policy determined by the Retail Stores Division management in Chicago. Our stores enjoy outstanding reputations for fashion, quality and service, and respond quickly to the customer needs in their market area. Our Men's Market and Women's Market Merchandising Corporations in New York act as buying offices and give our stores information on important fashion trends. The Division's management and staff provide important merchandising direction and advisory services. These include advertising, display, personnel, accounting, inventory control, systems and procedures, credit, tailoring and store leasing, construction, design and remodeling.

The Company plans to open 12 to 14 stores in 1977. During 1976, 17 stores were opened and five locations were closed. Three of the new stores, under the name R. J. Boggs, present a new internally developed concept to offer coordinated clothing and sportswear fashions in an exciting new setting designed to appeal to men in the 20 to 45 age group, the fastest growing segment of the population. The first three of these uniquely designed, smaller-space stores are in New Jersey. Several additional stores will be opened in the East in 1977. The new "Apostrophe" shops in Wallachs and several other stores were also developed to attract the younger, more fashion-conscious customer to our men's stores.

Women's wear volume, an important and growing part of our retail business, exceeds $85 million annually. The Company now operates 24 women's specialty stores, including four opened in 1976: Chas. A. Stevens with 16 in the Chicago area, J. P. Allen with 5 in Atlanta and deJong's with 3 in Evansville, Indiana. In addition, the number of women's departments in our 237 men's apparel stores was increased to 135 in 1976.

Our stores feature quality merchandise attractively displayed and provide the skilled personal service essential in selecting and fitting fashion apparel. Our stores appeal to the customer who appreciates fashion, quality and service.

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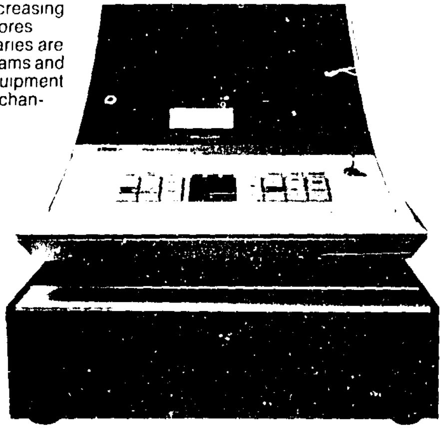
Substantial progress in computerizing various functions is contributing to ever-increasing efficiency in the retail stores Our major retail subsidiaries are using point of sale programs and supporting computer equipment to record sales and merchandising information



Interior of one of our new R J. Boggs stores shows how the entire store has been made into an attractive display which enables customers to choose a color-coordinated wardrobe with very little effort.

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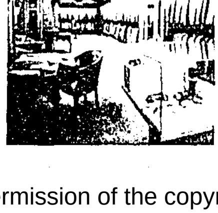
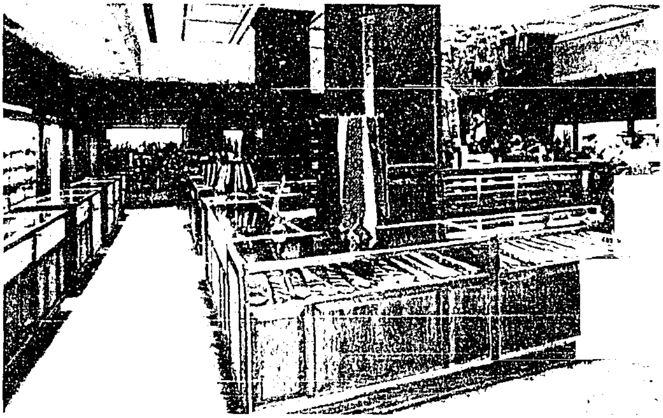
21 stores are operated by Baskin the leading men's specialty store in Chicago. Photos show the new Northbrook Court store, opened in 1976.

F R Tripler, Madison Avenue, New York has long been recognized as one of the finest men's wear stores in the world Among the fine men's apparel featured in this store is the largest collection of Hickey-Freeman suits in the country.





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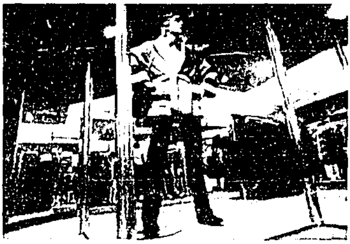
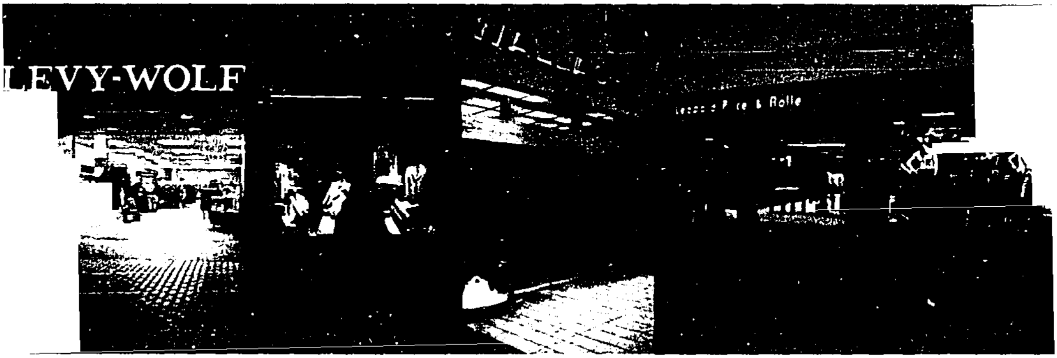
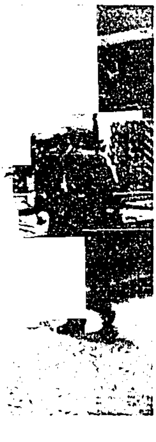
The flagship of the 24 store Wallachs operation is at 46th Street and Fifth Avenue in New York. The store was extensively remodeled in 1976. Additional space was added for the new "Apostrophe" shop designed to appeal to the young, fashion conscious customer.







The Levy-Wolf, Jacksonville and Leopold Price & Rolle, Houston stores shown here were opened in 1976. They are representative of a number of stores opened in several major growth areas across the country.

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Consolidated Statements of Earnings and Retained Earnings

Years ended November 30 (000's omitted)

Consolidated Statement of Earnings	1976	1975
Net sales	$534,609	$486,833
Other income	6,360	5,184
	540,969	492,017
Cost of goods sold	335,435	305,720
Selling, administrative and occupancy expenses	173,209	163,363
Interest expense	4,275	6,614
	512,919	475,697
Earnings before taxes	28,050	16,320
Taxes on earnings	14,200	8,010
Net earnings	$ 13,850	$ 8,310
Net earnings per common share and common share equivalent	$ 1.61	$ .97
Average number of common shares and common share equivalents	8,588	8,558

Consolidated Statement of Retained Earnings		
Retained earnings at beginning of year	$129,314	$126,212
Net earnings for the year	13,850	8,310
Cash dividends paid:		
Preferred shares, $2.00 per share	(164)	(164)
Common shares $.63 per share in 1976 and $.60 per share in 1975	(5,298)	(5,044)
Retained earnings at end of year	$137,702	$129,314

(See accompanying notes to consolidated financial statements)

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Consolidated Balance Sheet

		November 30 (000's omitted) 1976	1975
	Assets		
Current Assets	Cash and short term investments	**$ 16,248**	$ 14,330
	Accounts receivable, less allowance of $4,525,000 and $4,290,000 for doubtful accounts	**96,340**	87,649
	Inventories	**144,137**	126,637
	Prepaid expenses	**2,066**	2,243
	Total current assets	**258,791**	230,859
Other Assets	Other Assets	**4,030**	4,352
Properties	Land	**1,317**	1,317
	Buildings and building equipment	**13,795**	12,207
	Furniture, fixtures and equipment	**67,368**	64,385
	Leasehold improvements	**47,710**	46,971
		130,190	124,880
	Accumulated depreciation and amortization	**(74,827)**	(71,292)
	Net properties	**55,363**	53,588
		$318,184	$288,799
	Liabilities and Shareholders' Equity		
Current Liabilities	Notes payable to banks	**$ 14,000**	$ —
	Current maturities of long term debt	**940**	1,048
	Accounts payable and accrued expenses	**59,984**	52,791
	Taxes on earnings	**5,600**	642
	Deferred taxes on earnings	**3,240**	2,120
	Total current liabilities	**83,764**	56,601
Long Term Debt	Long Term Debt, less current maturities	**54,947**	61,136
Shareholders' Equity	Convertible preferred shares, $1 par value; authorized 2,500,000; issued and outstanding, Series A, 82,230	**82**	82
	Common shares, $2.50 par value; authorized 25,000,000; issued 8,676,520 in 1976 and 8,676,395 in 1975	**21,691**	21,691
	Capital surplus	**23,544**	23,544
	Retained earnings	**137,702**	129,314
		183,019	174,631
	Common shares in treasury, at cost, 267,414 in 1976 and 269,158 in 1975	**(3,546)**	(3,569)
	Shareholders' equity	**179,473**	171,062
		$318,184	$288,799

(See accompanying notes to consolidated financial statements)

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Consolidated Statement of Changes in Financial Position

Years ended November 30 (000's omitted)	1976	1975
Working capital was provided by:		
Net earnings for the year	$ 13,850	$ 8,310
Depreciation and amortization	7,514	7,718
Other	345	455
Working capital provided by operations	21,709	16,483
Proceeds from long term borrowing	17,050	–
	38,759	16,483
Working capital was used for:		
Payment of long term debt	23,239	14,209
Payment of dividends	5,462	5,208
Property additions—net	9,289	4,368
Purchase of treasury shares	–	182
	37,990	23,967
Increase (Decrease) in working capital	$ 769	$ (7,484)
Changes in components of working capital:		
Cash and short term investments	$ 1,918	$ 6,171
Accounts receivable	8,691	(8,263)
Inventories	17,500	(25,542)
Prepaid expenses	(177)	(631)
Accumulated income tax prepayments	–	(2,280)
Notes payable to banks	(14,000)	21,000
Current maturities of long term debt	108	(309)
Accounts payable and accrued expenses	(7,193)	4,016
Taxes on earnings	(4,958)	474
Deferred taxes on earnings	(1,120)	(2,120)
Increase (Decrease) in working capital	$ 769	$ (7,484)

(See accompanying notes to consolidated financial statements)

Report of Independent Accountants

To the Shareholders and Board of Directors of Hart Schaffner & Marx:

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of earnings, retained earnings and changes in financial position present fairly the financial position of Hart Schaffner & Marx and its subsidiaries at November 30, 1976 and 1975, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

Price Waterhouse & Co.

Chicago, Illinois
January 18, 1977

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Notes to Consolidated Financial Statements November 30, 1976 and 1975

Summary of accounting policies

The consolidated financial statements include the accounts of the Company and all subsidiaries

Inventories are stated at the lower of cost or market. Cost is determined by the use of the first-in, first-out method for the majority of the inventory, although for a substantial amount, the last-in, first-out (LIFO) method is used. The excess of current costs over LIFO costs for certain manufacturing inventories increased during 1976 by $1.6 million; if current costs had been used, inventories would have been $3.4 million higher than reported at November 30, 1976, compared to approximately $1.8 million higher at both November 30, 1975 and 1974.

Properties are stated at cost. Additions, major renewals and betterments are capitalized, maintenance and repairs which do not extend asset lives are charged against earnings. Profit or loss on disposition of assets is reflected in earnings and the related asset costs and accumulated depreciation are removed from the respective accounts except for certain assets for which the composite method of computing depreciation is used under which no gain or loss is recognized on disposition.

Accelerated depreciation methods are used for a significant portion of the properties and the straight line method is used for the remainder. Depreciation is computed based on useful lives of 20 to 45 years for buildings, 5 to 20 years for building equipment and 3 to 15 years for furniture, fixtures and equipment. Amortization of leasehold improvements is based upon the terms of the respective leases.

Deferred taxes on earnings are provided for timing differences between financial and taxable income. Investment tax credits are recognized as a reduction of the current provision for taxes on earnings in the year the related assets are placed in service.

The Company and its subsidiaries maintain pension plans covering substantially all employees other than those covered by union-sponsored plans. Pension expense charged against earnings includes current service costs and, as to plans not fully funded, amortization of prior service costs over periods ranging from ten to thirty years. Pension costs are funded as accrued and the amounts funded at November 30, 1976 exceeded the actuarially computed total of vested benefits.

Earnings per share are computed based on the average number of common shares and common share equivalents outstanding. Convertible preferred shares have been included as common share equivalents. When dilutive, stock options are included as share equivalents using the treasury stock method.

Leases

At November 30, 1976, the Company and its subsidiaries were committed under noncancelable leases, covering primarily retail properties, which require total minimum annual rentals and rentals applicable to capital leases as follows (000's omitted):

Years	Capital leases	All leases
1977	$ 698	$12,571
1978	698	11,907
1979	698	11,269
1980	698	11,010
1981	698	10,352
1982-1986	4,235	42,807
1987-1991	3,566	25,185
1992-1996	875	7,513
Thereafter	1,699	2,146

Over 90 percent of all leases provide for the payment by the lessors of all or most of the applicable real estate taxes, maintenance and insurance costs, which are substantial in proportion to the minimum rentals. Minimum rental income from noncancelable subleases offset against the above total rentals is $617,000 in 1977 and progressively less in subsequent years.

Rental expense, including rentals under short-term leases, was comprised of the following (000's omitted):

	1976	1975
Capital leases:		
Minimum rentals	$ 877	$ 888
Contingent rentals	100	100
Sublease (income)	(204)	(182)
Operating leases:		
Minimum rentals	13,894	13,745
Contingent rentals	4,403	3,468
Sublease (income)	(699)	(677)
Total rental expense	$18,371	$17,342

Almost one-half of the leases contain renewal options ranging from 5 to 25 years; several leased facilities may be purchased at various dates at an aggregate cost of $5,500,000. Contingent rental payments are generally based on the sales volume of the rental unit.

The present value of capital lease commitments was $6.5 million at November 30, 1976 and $6.8 million at November 30, 1975. The weighted average of interest rates used to compute present value was approximately 5.1 percent in both 1976 and 1975. The range of interest rates was 3.5 to 7.5 percent in both years.

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The Financial Accounting Standards Board recently issued a statement concerning Accounting for Leases. Certain leases previously classified as non-capitalized financing leases have been reclassified as operating leases in conformity with the statement. The statement includes a requirement, not yet effective, that the present value of capital leases be retroactively recorded as fixed assets and liabilities in the future. Had the rental properties which are classified as capital leases been capitalized, amortized and interest accrued on the basis of the outstanding lease commitments, the effect on net earnings in 1976 and 1975 would have been insignificant.

Taxes on Earnings

The provision for taxes on earnings is summarized as follows (000's omitted):

	1976	1975
Current		
Federal	$10,650	$2,490
State and other	1,730	420
Foreign	700	700
Total current	13,080	3,610
Deferred		
Federal	970	3,800
State and other	150	600
Total deferred	1,120	4,400
Total taxes on earnings	$14,200	$8,010

The deferred tax provisions are primarily comprised of $1,100,000 and $1,300,000 in 1976 and 1975, respectively, attributable to deferred gross margin on installment sales and $2,800,000 in 1975 applicable to gross margin on intercompany inventory.

The effective tax rate was 50.6% in 1976 and 49.1% in 1975. The difference between total taxes on earnings reflected in the accompanying statement of earnings and the amount computed by applying the federal statutory tax rate to pre-tax earnings is summarized as follows:

	Percent of pre-tax earnings	
	1976	1975
Taxes computed at statutory rate	48.0%	48.0%
State and other taxes on earnings net of federal tax benefit	3.5	3.3
Investment tax credit (Approximately $500,000 in 1976 and $300,000 in 1975)	(1.8)	(1.8)
Other—net	.9	(.4)
	50.6%	49.1%

Long Term Debt

At November 30, 1976 and 1975, long term debt, less current maturities, was comprised of the following (000's omitted):

	1976	1975
Notes payable to banks under credit agreement	$ —	$21,000
8½% sinking fund debentures (due 1996)	32,700	35,000
9¼% promissory notes (due 1991)	17,050	—
Other debt, extending to 1991 (average interest rate of 5½%)	5,197	5,136
	$54,947	$61,136

At November 30, 1976, $14,000,000 of notes payable to banks under the credit agreement were outstanding but were classified as current liabilities because all $14,000,000 had been paid and the agreement terminated in December, 1976.

Annual retirements of $1,750,000 of the 8½% sinking fund debentures are required commencing in 1978 During 1976, the Company purchased $2,300,000 principal amount of the debentures which is shown as a reduction of long term debt. The Company is permitted to apply this amount toward the sinking fund requirement.

In October, 1976, the Company entered into a note agreement with several institutional investors which provides for $25,000,000 of borrowings evidenced by 9¼% promissory notes. Of this amount, $17,050,000 was received on October 15, 1976, and the agreement provides for the remaining $7,950,000 to be received in 1977. The notes require annual payments of $1,400,000 on December 1, 1981, 1982 and 1983 and $2,600,000 annually each December 1 thereafter. The Company may make optional prepayments without premium in amounts equal to and at the dates of the required payments, not to exceed $7,500,000 in the aggregate, and may make additional prepayments, subject to certain restrictions prior to November 1, 1985, of all or any portion of the notes at varying premiums.

Under the most restrictive provisions of the Company's several borrowing agreements, the Company may incur total funded debt up to approximately the amount of shareholders' equity, and at November 30, 1976 senior funded debt was limited to approximately $160 million. In addition, at November 30, 1976 consolidated working capital was $175 million compared to $83 million required to be maintained by the Company. Consolidated retained earnings of $20,600,000 at November 30, 1976 plus 80% of earnings thereafter are available for the payment of future cash dividends.

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Stock Option Plans

The Company has stock option plans under which officers and key employees may be granted options to purchase the Company's common stock at prices equal to the fair market value at date of grant. Options under all plans are exercisable to the extent of 25% each year (cumulative) from the second through the fifth year, and expire five to ten years after date of grant. A total of 464,381 common shares were reserved at November 30, 1976 for options granted or to be granted.

A summary of the plans for the year ended *November 30, 1976 is as follows:*

	Number of shares under option	Range of option prices per share
Under option, at beginning of year	410,995	$6.38 to $31.25
Granted	*81,550*	*9.94 to 13.57*
Exercised	(125)	6.57 to 10.07
Expired or terminated	(104,810)	6.63 to 31.25
Under option at end of year	387,610	6.38 to 30.00 (average of $14.95)

		Available for grant:	
Options exercisable at end of year	162,632	Beginning of year	57,664
		End of year	76,771

Pension Plans

The Company's principal plan requires contributions by the employees and another pension plan permits voluntary employee contributions. Except for several deferred profit sharing plans of subsidiaries, all employer contributions are based on actuarial determinations.

Total pension costs for each of the years ended November 30, 1976 and 1975 were approximately $2,650,000, excluding contributions to union-sponsored plans. Unfunded past service liability at November 30, 1976 was approximately $1,900,000.

Consent Decree

A consent decree entered on June 1, 1970 by the United States District Court requires either consent of the Department of Justice or approval of the Court to acquire an interest (or assets) in any existing men's clothing store prior to June 1, 1980. The last divestiture *requirements of the decree were satisfied* in 1974.

Convertible Preferred Shares

Series A preferred shares are voting shares, each convertible into 1.8 common shares and are cumulative with an annual $2 dividend rate. The shares are callable at a liquidation price of $67.50 each (an aggregate of $5,551,000 at November 30, 1976) and 148,014 common shares are reserved for conversion.

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Management's Discussion and Analysis of the Consolidated Summary of Operations

Consolidated sales reached a record high of $535 million in 1976 compared to $423 million in 1972. Sales increased each year except 1975, when the apparel industry was adversely affected by the recession and our manufacturing sales were lower. The Retail Stores Division sales increased to $337 million in 1976 from $275 million in 1972. During this five-year period, 53 stores were opened and almost the same number of stores were sold or closed including 30 men's stores divested under a consent decree. Retail sales in 1975 increased slightly even though fewer stores were operated following the sale of 22 stores during 1974, when the last divestiture requirements of the decree were satisfied.

Manufacturing sales to independent accounts were 37 percent of consolidated sales or approximately $200 million in 1976, an increase of one-third over the 1972 sales of approximately $150 million. Manufacturing shipments to our stores also increased proportionately, and ranged between 22 and 27 percent of the total manufacturing production during the five years. Men's apparel produced by the Company's manufacturing divisions represents approximately 40 percent of the men's apparel sold in our retail stores. Retail suit prices of the Company's brands are shown for the current season on the graph.

In 1976, sales increased $47.8 million or 9.8 percent over 1975, when sales decreased 1.6 percent. Improved economic conditions and the renewed interest in quality apparel benefited manufacturing and retailing. Manufacturing sales increased 13 percent to a record high and the Retail Stores Division also enjoyed record sales with an increase of almost 9 percent over 1975.

During each quarter of 1976, earnings rebounded sharply compared to 1975, when only the fourth quarter showed an earnings improvement. Earnings before taxes increased 72 percent from $16,320,000 in 1975 to $28,050,000 in 1976, which is within 10 percent of the 1973 earnings before taxes. Net earnings increased 67 percent to $13,850,000 in 1976, after decreasing 29 percent in 1975 to $8,310,000 from $11,755,000 in 1974. Earnings per share were $1.61 in 1976 compared to 97 cents in 1975, $1.36 in 1974 and record earnings of $1.84 in 1973.

The Retail Stores Division and the manufacturing divisions both contributed to the higher consolidated earnings in 1976, compared to 1975 when both divisions experienced lower earnings. Gross margins improved from 1975, when it was not possible to offset higher costs under depressed pricing conditions. The last-in, first-out (LIFO) method of accounting for inventory, which charges cost of goods sold with current costs, was adopted for certain manufacturing inventories in 1974. The excess of current costs over LIFO costs increased during 1976 by $1.6 million; if current costs had been used, inventories would have been $3.4 million higher than reported at November 30, 1976, compared to approximately $1.8 million higher at November 30, 1975 and 1974.

Selling, administrative and occupancy expenses increased $9.8 million to $173.2 million in 1976 from $163.4 million in 1975. However, the expense ratio was lower. Expenses in both manufacturing and retailing were reduced as a percent of sales. Inflationary pressures caused expenses in 1975 to increase $3.4 million over 1974. Continued controls improved 1976 to approximately the same ratio as 1974.

Interest expense decreased to $4,275,000 in 1976 compared to $6,614,000 in 1975 and $6,979,000 in 1974. Most of the decrease resulted from lower bank borrowings during the first half of 1976, when inventories were unusually low. In October 1976, the Company entered into an agreement to borrow $25 million from several insurance companies; $17 million was received on October 15, 1976, and the remaining $8 million is to be received in May 1977. All remaining indebtedness to banks was paid in December 1976, when the long-term bank credit agreement was terminated, and 1977 seasonal needs will be financed with short-term borrowings. The Company is in an excellent financial position to take advantage of the growing market for apparel sales in the years ahead.

Form 10-K: Hart Schaffner & Marx will provide to any shareholder, without charge, a copy of its Annual Report on Form 10-K, as filed with the Securities and Exchange Commission (but without exhibits). Requests should be in writing to: Hart Schaffner & Marx, attention: Mrs. Kay C. Nalbach, Assistant Secretary, 36 South Franklin Street, Chicago, Illinois 60606.

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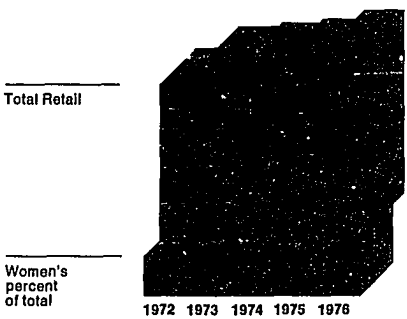
Five Year Consolidated Summary of Operations
(000's omitted)

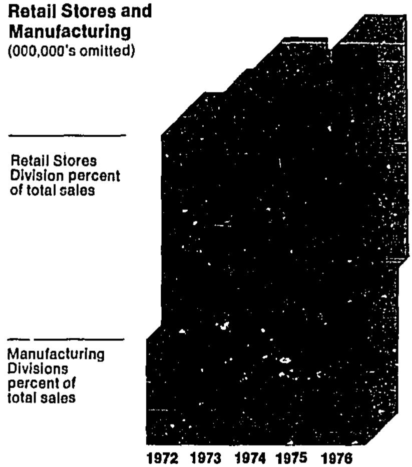
	1976	1975	1974	1973	1972
Net sales	**$534,609**	$486,833	$494,937	$469,158	$423,114
Cost of goods sold	**335,435**	305,720	310,150	286,470	259,093
Interest expense	**4,275**	6,614	6,979	4,873	3,996
Earnings before taxes	**28,050**	16,320	23,146	30,422	27,214
Taxes on earnings	**14,200**	8,010	11,391	14,297	13,024
Net earnings	**13,8[illegible]0**	8,310	11,755	16,125	14,190
Net earnings per common share and common share equivalent	**1.61**	.97	1.36	1.84	1.61
Cash dividends paid on: Preferred shares	**164**	164	164	164	180
per share	**2.00**	2.00	2.00	2.00	2.00
Common shares	**5,298**	5,044	7,466	7,414	6,914
per share	**.63**	.60	.88	.86	.80
Average number of common shares and common share equivalents	**8,588**	8,558	8,637	8,767	8,805

Sales

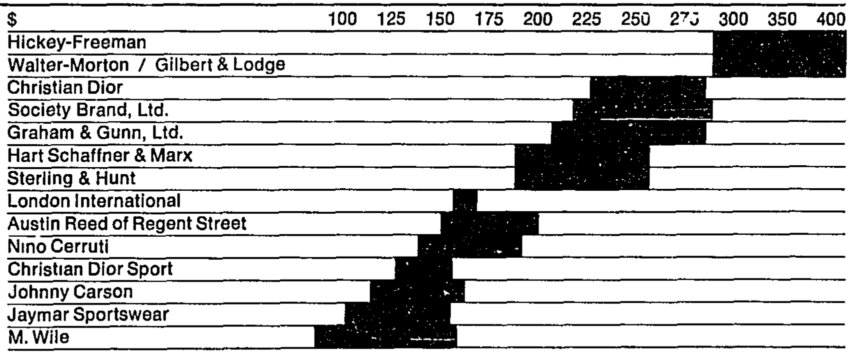
Retail Stores
(000,000's omitted)



Retail Stores and Manufacturing
(000,000's omitted)



Retail Price Ranges of Suits by Brand



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Retail Stores Division

Robert J. Witt, *President*
Harry P. Guinther, *Executive Vice President*
Charles A. DeChants, *Senior Vice President*
Don A. Miller, *Senior Vice President*
Henry C. (Chick) Schwartz, *Senior Vice President*
Frank Brenner, *Vice President*
Gene Coccodrilli, *Vice President*
Gerard K. Donnelly, *Vice President*
Donald R. Putnam, *Vice President*

Men's Market Merchandising Corporation

Matthew F. Shannon, *President*
Allan Baumel, *Vice President*
Eugene L. Mellott, *Vice President*

Women's Market Merchandising Corporation

Betty Green, *President*

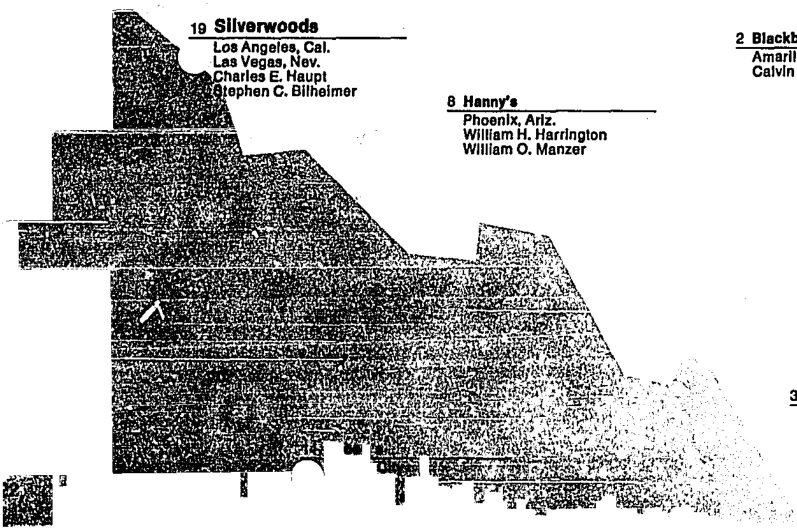
7 Klopfenstein's
Seattle-Tacoma, Wash.
Anchorage, Alaska
Hugh C. Klopfenstein

1 Littler
Seattle, Wash.
Laurence Fry

4 Rosenblatt's
Portland, Ore.
Bruce Bailey
Hugh C. Klopfenstein

15 Hasting's
San Francisco, Cal.
Sacramento, Cal.
Enzo Belli

19 Silverwoods
Los Angeles, Cal.
Las Vegas, Nev.
Charles E. Haupt
Stephen C. Bilheimer



3 Arthur Frank
Salt Lake City, Utah
Lawrence K. Goldsmith
Simon Frank

8 Hanny's
Phoenix, Ariz.
William H. Harrington
William O. Manzer

1 Waymires
Colorado Springs, Col.
Jack Waymire

5 Liemandt's
Minneapolis, Minn.
John A. Liemandt

2 Kucharo's
Des Moines, Iowa
Nate Bernstein

4 Jack Henry
Kansas City, Mo.
David M. Carpenter
Ernest A. Dick

2 Ray Beers
Topeka, Kan.
Ray Beers, Jr.
Philip C. Gibson

2 Blackburns
Amarillo, Tex.
Calvin McAdams

8 Jas. K. Wilson
Dallas, Tex
Alex J. Cochrane

2 Washer Bros.
Ft. Worth, Tex.
Donald G. Noel

2 Merritt Schaefer & Brown
Austin, Tex.
Ronald Kercheville

8 Leopold Price & Roll
Houston, Tex.
Harvey Brown

3 Frank Bros.
San Antonio, Tex.
Earl H. Freeman
Stanley Frank, Sr.

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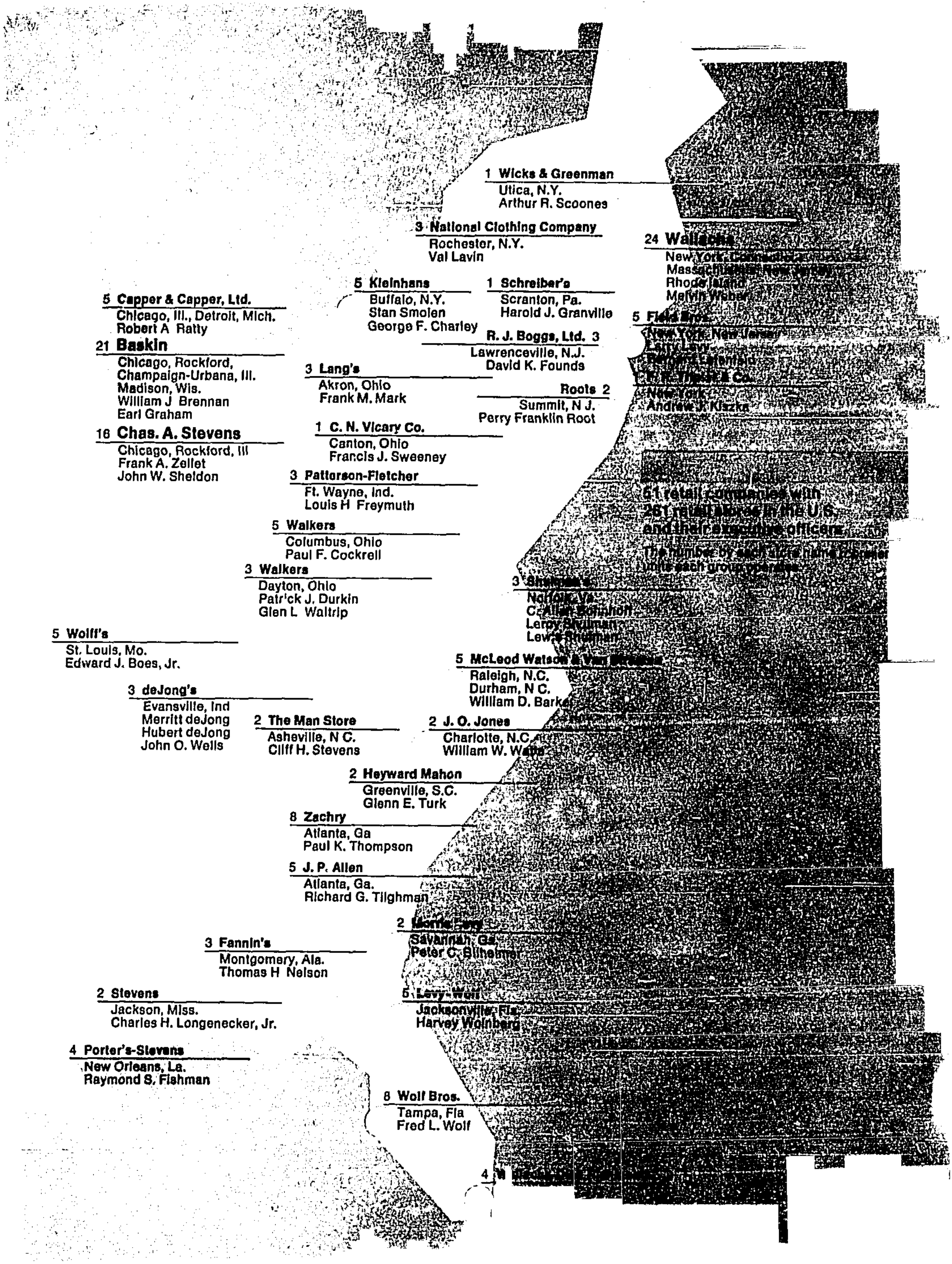

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Hart Schaffner & Marx Clothes

Hart Schaffner & Marx
Christian Dior
Sterling & Hunt
Jack Nicklaus
Graham & Gunn, Ltd.

Society Brand, Ltd.

Austin Reed of Regent Street

Fashionaire

Suits, sport coats, slacks, and outercoats

36 South Franklin Street
Chicago, Ill. 60606

8 Plants: Chicago (3) and Rock Island (2), Ill.; Rochester, Ind ; and Cape Girardeau and Chaffee, Mo.

M. Wile & Company, Inc.

Nino Cerruti
Don Richards
Country Casuals
London International

Johnny Carson

Suits and sport coats

2020 Elmwood Avenue
Buffalo, N.Y. 14207
3 Plants: Buffalo (2) and Dunkirk, N.Y.

Jaymar-Ruby, Inc.

Jaymar
Cary Middlecoff
Sansabelt
Nino Cerruti Sport

Slacks, sport coats and coordinated sportswear

5000 South Ohio Street
Michigan City, Ind. 46360
9 Plants. Michigan City (4) and East Chicago, Ind.; Anniston and Russellville, Ala.; Elizabethtown, Ky.; and Rector, Ark.

Hickey-Freeman Co., Inc.

Hickey-Freeman
Walter-Morton
Gilbert & Lodge

Suits, sport coats, slacks, outercoats and formalwear

1155 Clinton Avenue North
Rochester, N Y 14621
3 Plants: Rochester (2) and Buffalo, N.Y.

Gleneagles, Inc.

Gleneagles
Great Western

Rainwear, outerwear, sportswear and leisurewear

808 Gleneagles Court
Baltimore, Maryland 21204
3 Plants: Baltimore and BelAir, Md., Chisholm, Minnesota

Blue Jeans Corporation

BJC
Hallsboro
Corn Cobbers

Jeans and coordinated outfits

130 West 34th Street
New York, N.Y. 10001
2 Plants· Whiteville, N C. and Bethune, S.C.

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William H Mier, *President*
E O Hand, *Executive Vice President*
Thomas J. Flavin, *Group Vice President*
Alfred Katz, *Group Vice President*
Hugh Gallarneau, *Vice President*
Max A Hart, *Vice President*
Anthony Karson, *Vice President*
Michael Kent, *Vice President*
William R Loeffler, *Vice President*
William W. Rowlette, *Vice President*
Donald D Shorr, *Vice President*
Al Bergschneider, *Controller*

Society Brand, Ltd.

Suits, sport coats and slacks

Howard Zenner, *Executive Vice President*
Herbert C Wallace, Jr , *Vice President*

Austin Reed of Regent Street

Suits, sport coats, slacks, weatherwear and sportswear

Barry A. Reed, *Chairman and President*
Robert E. Bruno, *Executive Vice President*

Fashionaire

Men's and women's career apparel

Barbara Ash, *Vice President*
Edgar Stern, *Vice President*

Arthur Gunzberg, *Chairman*
Lawrence Gunzberg, *President*
Kenneth Hoffman, *Executive Vice President*
Guy Gunzberg, *Senior Vice President*
Anthony Caine, *Vice President*
Joseph Diskin, *Vice President*
Harry Feldstein, *Vice President*
Norbert Huber, *Vice President and Secretary*
Frank Norton, *Vice President*
George Odvarka, *Vice President*
Fred Pepperday, *Vice President*
Edward Robbins, *Vice President*
Joseph Starzec, *Vice President*

Johnny Carson Apparel, Inc.

Suits, sport coats, weatherwear and furnishings

Arthur Gunzberg, *Chairman*
Johnny Carson, *President*
Kenneth Hoffman, *Vice President*

J M. Ruby, *Chairman*
Burton B Ruby, *President*
William E. Staples, *Group Vice President*
Nathan S. Balser, *Vice President*
Jack R. Frank, *Vice President*
Hartley Job, *Vice President*
Al E Kahan, *Vice President*
Edwin H Levitin, *Vice President*
Harold Leinwand, *Vice President and Treasurer*
James J. Moore, *Vice President*
Gerald I Paige, *Vice President*
Robert L Plummer, *Vice President*
Roger L. Webb, *Vice President*

Walter B D Hickey, Sr., *Chairman*
Walter B. D Hickey, Jr , *President*
Richard B Lyons, *Vice President*
Morris M Medved, *Vice President*
Howard A Breiterman, *Vice President*
G Sheldon Brayer, *Vice President*
Aime G Messe, *Vice President & Secretary*
Donald B. Parish, *Treasurer*

Charles R Lamm, *Chairman*
Lawrence F. Nein, *President*
J Roger Holland, *Executive Vice President*
Alfred S Oppenheimer, *Senior Vice President*
Carl W. Sand, *Vice President and Controller*
David H Schmidt, *Vice President*
James R Swann, *Vice President*

Also rainwear, outerwear and sportswear under labels of Christian Dior, Jack Nicklaus, Nino Cerruti and Johnny Carson.

Stanley Goldberg, *President*
Seymour Elkins, *Vice President*
P Douglas McMillan, *Vice President and Treasurer*
Martin Steinberg, *Vice President*

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